In the Supreme Court of the United States

OCTOBER TERM, 1953

No. 111

SECURITIES AND EXCHANGE COMMISSION, PETITIONER

v.

JAMES F. MASTERSON

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

REPLY OF SECURITIES AND EXCHANGE COMMISSION, PETITIONER, TO BRIEF IN OPPOSITION

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1. Respondent suggests that there is no general importance to the problem of the Commission's powers with respect to fees, or the scope of judicial review thereof, because the program of corporate simplification directed by the Holding Company Act has been substantially completed (Br. in Opp., pp. 27-28). However, this progress toward completion of the simplification program has brought to the fore the questions involved in evaluating the

services rendered in the reorganization proceedings.

Since June, when the petition was filed, additional applications for compensation totalling approximately $5,750,000 have been filed with the Commission. During this period, the Commission has acted upon approximately $3,500,000 of claims. The total amount of fee claims pending before the Commission is now approximately $10,500,000,[1] including claims of persons retained by companies subject to regulation amounting to approximately $2,500,000. There are now seven fee cases pending in the lower courts involving review of Commission allowances in Section 11(e) proceedings.

2. Respondent disputes the Commission's statement of the questions presented, and argues that this case presents no more than a holding by the courts below that, on the basis of the particular facts, the Commission acted arbitrarily. We recognize that both courts below expressly relate their holdings to the facts of the case. But, as stated in the petition, the one "fact" stressed by the District Court—in what the Court of Appeals concluded to be a proper exercise of its review jurisdiction—was the holding company client's opinion as to the worth of Masterson's services, to which the Commission was required to give "full weight." There was no judicial finding, and we believe no record basis, for concluding that, if the Commis-

[1] This figure does not include applications for reimbursement of expenses totalling approximately $475,000.

sion was authorized to perform the primary act of valuation and judgment with respect to the worth of these services, it could not rationally have arrived at the amount allowed by it, or indeed at any intermediate sum less than that to which the management and Masterson had agreed.

The brief in opposition appears to us to confirm our own analysis of the holdings below, as denying to the Commission the customary authority of other first instance reorganization tribunals with respect to fees, and leaving it without effective control thereof. That the Commission lacks power to determine fees within the area where there is room for reasonable differences of judgment is a premise which underlies respondent's factual argument. The very statement of the gist of the District Court's holding assumes that it is management rather than the Commission which has primary responsibility for judgment in this area. Thus it is stated (p. 16) that the District Court held no more than that "the specific agreement . . . was arbitrarily brushed aside by the SEC in the face of the record evidence establishing both the fairness and the reasonableness of the agreement." This argument does not really join issue with the Commission in view of its concession in the court below (quoted in the petition, p. 18) that the Commission did not claim that it would be improvident for management to agree, or an abuse of discretion for the District Court to approve, the sum allowed, if either had primary power to exercise discretion with respect to the fee.

Much of respondent's factual argument is irrelevant to the precise question at issue, and goes to show merely that the Commission properly awarded Masterson some fee, not that it lacked a reasonable basis for judgment that an appropriate fee was lower than that which management was prepared to pay. Thus, respondent argues (p. 16) that the court below properly concluded that under the circumstances "it was in the best interest of Light and Power to be represented by more than one attorney." The Commission, of course, did not act on any inconsistent hypothesis. Again, respondent relies (p. 18) upon the combined contribution of Kline and Masterson to the proceeding, but points to no finding by the District Court that the total amount the Commission allowed to both Kline and Masterson was inadequate or that the Commission exceeded the limits of rational judgment in estimating the relative contributions of Kline and Masterson. Respondent argues further that the level of compensation which the enforcement court directed to be paid him "was reasonable and indeed modest in relation to the scale of attorneys' compensation which the SEC itself" allowed other counsel. But respondent does not undertake to show any basis for concluding, nor suggest that the District Court concluded, that the Commission was unreasonable in its allowance of approximately $2,000,000 for the total of lawyers' fees in the reorganization. Nor did it direct a reallocation as between Master-

son and other counsel. The possibility, insinuated by respondent, that the Commission may have been guilty of what is sometimes referred to as "vicarious generosity" in its award to other fee claimants, hardly makes it a proper exercise of the district court's review function to engage in a similar generosity for respondent's benefit. Indeed there is no suggestion in the District Court's opinion that it relied on such considerations except to show that the Commission was not on firm ground in differing with management.

Respondent also tenders, as a factual argument, various reasons why the managements of the companies concerned and the District Court were better qualified than the Commission to judge the worth of his services, viz., "the managements . . . had an intimate first-hand knowledge of Masterson's services rendered without as well as inside the hearing room" (p. 18). It is further argued that a judicial person is inherently better qualified to determine the worth of lawyers' services than a quasi-judicial person which in some respects is itself a litigant (p. 33); that the Commission, and its staff, are more likely to be impressed with lawyers who argue in accordance with than in opposition to their own views (p. 34); that "charges of favoritism" have been leveled at the Commission; that any claim on the Commission's part to exercise authority over fees within the area where there is room for reasonable differences of judgment is a claim to "dictatorial

and non-reviewable powers" (p. 29);[2] that a commission whose members are not necessarily lawyers cannot be expert as to fees, while the district judge here involved was particularly expert.

Some of these arguments find their parallel in that portion of the District Court's initial opinion which deprecated the Commission's ability to reach a conclusion as to the "duplicative and secondary character of the services" rendered by Masterson (R. 79), and characterized as "avowed paternalism" and not in accord "with legal standards" the Commission's unwillingness to accept management's judgment. We find no suggestion in the District Court's opinion, however, that it claimed for itself any special qualifications to exercise a direct and informed judgment as to the worth of Masterson's services. The Court relied on its own experience only to conclude that Masterson, as additional counsel might have rendered more valuable services than was apparent from anything that appeared in the record of the reorganization, and that therefore the Commission was not warranted in rejecting the company's

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[2] *Cf. Reconstruction Finance Corp.* v. *Bankers Trust Co.*, 318 U.S. 163, at p. 170, where it is stated concerning the respective functions of Commission and court in passing upon railroad reorganization fees:

> Our conclusion is that the function committed by the law to the Commission is the ordinary one reposed in a fact finding body and that its findings, supported by evidence, may not be disturbed by a court. This construction of the Act leaves the court free to decide upon the basis of the Commission's report all questions of law. With respect to the amount set as a maximum the only question of law which can arise is whether there is substantial evidence to support the Commission's finding.

judgment. Both the reasoning of the District Court, and the exact coincidence between its directions to the Commission on remand and the agreement, show that it did not attempt to exercise the primary judgment as to the worth of the services which was denied to the Commission. Thus, as we argue more fully in the petition, the decision denies the Commission real powers of regulation with respect to reorganization fees without substituting judicial regulation of the type exercised in Chapter X proceedings.

3. Respondent's brief (pp. 37-40) refers to Commission and court comment on the powers and responsibilities of management in Section 11 proceedings. All of the citations, however, deal with the exclusive power of the management, *vis-a-vis* individual security holders, to initiate proceedings and submit proposals. None of them suggests any special weight to be given to management valuations, whether of securities or of services. The latitude of the regulated companies in formulating and presenting plans, and in retaining counsel of their own choice, is no limitation on the power and duty of the Commission to determine independently the fairness of the plans and the value of the services rendered. It is the Commission's valuation findings, not those of the regulated companies, which are to be upheld by the courts if supported by substantial evidence. *S.E.C.* v. *Central-Illinois Securities Corp.*, 338 U.S. 96, 125.

4. Respondent urges that the decision below cannot be interpreted as denying the Commission

effective control of fees to the extent agreed to by a holding company client, because in *Matter of Public Service Corporation of New Jersey,* Holding Company Act Release No. 12,000, the Commission did not construe the decision "to mean that this Commisson cannot determine the amount of a reasonable fee to be less than that agreed to by the company and its counsel." The brief in opposition omits the fact that the company counsel have pending in the Third Circuit a petition to review the ruling of the Commission reducing their fee from $150,000 to $125,000.

One of the major problems created by the decisions below is their impact on the review process. They constitute an invitation to fee claimants to challenge, and to the reviewing courts to upset, any decision of the Commission allowing less than the amount which a management has agreed to pay, unless the Commission can sustain the burden of proving that the agreed amount is unreasonable, unfair, excessive, or arbitrary. The effectiveness of the Commission's regulation of fees in Section 11 reorganizations depends not only on the Commission's treatment of agreements between regulated companies and their counsel, but more importantly upon the standards applied by the reviewing courts in determining whether to uphold or to disregard the Commission's judgment. The problem is well illustrated in the *Northern States* case.[3] There the enforcement court, in an

[3] *In re Northern States Power Company* (unreported), D. Minn., Civil Action No. 2673, January 12, 1953, pending on appeal, C.A. 5.

opinion reflecting essentially the views of the District Court in the instant case, rejected the Commission's fee allowances as inadequate in four instances where the Commission had allowed less than the amounts the companies in reorganization had undertaken to pay, and with respect to company counsel directed payment of the precise amounts approved by the companies. In discussing the claims of one of the company counsel, the Court commented that the fees claimed "cannot be characterized as being so unreasonable that good conscience requires their denial." This is essentially the test applied by the District Court and affirmed by the Court of Appeals below, and which the Commission is now testing on appeal in the *Northern States* case.

5. In the case below, as in substantially all of the pending litigation on fees in Holding Company Act reorganizations, the claims of company counsel are considered by the managements of the companies in reorganization, by the Commission, and frequently, in the event of a difference of judgment between them, by the reviewing court. As we read the Act and its legislative history, the statutory scheme contemplates that the Commission's evaluation of the services rendered shall prevail, unless that judgment is shown to be arbitrary and not supported by substantial evidence. The decisions below require the Commission to demonstrate that the more generous appraisals of man-

agement are unreasonable, in order for its judgment to prevail. This is an important issue in the administration of the Act, and should be reviewed by this Court.

Respectfully submitted,

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v.

JAMES F. MASTERSON,
Respondent.

RESPONSE TO REPLY OF SECURITIES AND EXCHANGE COMMISSION

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RESPONSE TO REPLY OF SECURITIES AND EXCHANGE COMMISSION

In its Reply Brief, Petitioner continues the process commenced in its Petition, of attempting to obtain *certiorari* in this case on the basis of its contentions as to issues presented by the *Northern States* and other cases pending undecided before various lower courts. We have heretofore commented on this extraordinary procedure, and have also pointed out that such cases are in a great many significant respects dissimilar to the case at bar.[1] If those cases actually do present the issues on which Petitioner seeks to have this Court pass, that constitutes no justification for requesting the Court to pass upon them *anticipatorily* in the instant case, where such issues are not in fact presented and the facts are very different.

Petitioner persists in its attempt to manipulate the decisions of the Courts below into a holding that arms-length compensation agreements between companies and their counsel may not be overridden unless the Commission has succeeded in "demonstrating" that the agreement is unreasonable. It may be that there is a good deal to be said in favor of such a doctrine, if due regard be given to the particular nature of Section 11 (e) proceedings;[2] but such was *not* the holding of the Courts below in this case.

In the case at bar, the Enforcement Court regarded the managerial judgment as one evidentiary factor to be considered, but it examined and assessed that evidentiary factor *in the light of the record evidence as a whole.*[3] As the Court of Appeals stated upon its own consideration of the record, made in the light of Petitioner's contentions similar to those here presented, the holding of the Enforcement Court was merely that the SEC'S determination "was not just and reasonable . . . *in all the circumstances of this case.*"[4]

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[1]Brief in Opposition, pp. 21-27.

[2]Indeed, as we have previously pointed out, this is virtually the doctrine enunciated by the SEC itself, in its brief before Judge Leahy in the *Engineers* case; Brief in Opposition, pp. 37-39.

[3]See Brief in Opposition, pp. 16-21.

[4]202 F 2d at p. 639 (emphasis supplied).

It is thus evident that what Petitioner really seeks is that this Court should now override or discard those principles of appellate review several times enunciated and reaffirmed during the last several terms, that:

> "[C]ongress charged the Courts of Appeal, not this Court, with the normal and primary responsibility for reviewing the conclusions of the Board . . .
> [T]his Court is not the place to review a conflict of evidence nor to reverse a Court of Appeals, because were we in its place we would find the record tilting one way rather than the other, though fair-minded judges could find it tilting either way . . . We repeat and reaffirm this rule, noting its special applicability to cases where, as here, a statutory standard such as 'good faith' *can have meaning only in its application to the particular facts of a particular case.*" (*Labor Board v. American Insurance Co.*, 343 U.S. 395, 409-410; Emphasis supplied)

We submit that this does not present a meritorious issue which justifies issuance of *certiorari*, or the imposition of further delay and expense on respondent.

Dated: October 2, 1953

Respectfully submitted,

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Attorney for Respondent